

Co-operative Governance

Public policy debate has in recent years increasingly focussed on the governance of business enterprises. Large co-operatives incorporated under Corporations Law are equally impacted by this debate.

Unfortunately, the values underpinning this debate assume investor ownership and control of these enterprises. It is critical, therefore, to consider the specifics of governance for co-operatives.

Co-operative governance is the set of relationships between the co-operative's members, the board as representatives of members that advise management for the members and the management that has the care and control of the co-operatives and how a business can be best governed in the interests of its owners.

Co-operative governance also provides the structure through which the objectives of the co-operative are set and the means of attaining those objectives and the monitoring of performance.

Co-operative governance is different from the governance of investor-owned and public enterprises. Good co-operative governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the co-operative and members and should facilitate effective monitoring, thereby encouraging the co-operative to use resources more effectively. Co-operatives differ from investor-owned companies in their:

- character
- purpose
- goal-setting
- methods of financing
- profit distribution

Governance in an investor-owned company is aligned with profit maximization. Co-operative governance, however, is broader and more complex than profit and is based on co-operative values and principles. A commitment to co-operative governance improvement is particularly important for co-operatives because they are not exposed to the "disciplines" of the stock exchange. Understanding and embracing co-operative governance is essential for the strategic re-positioning of co-operatives to survive globalization and the challenge of investor-owned companies and, in particular, multinationals. Fundamental to this, however, is acknowledgement of the strategic and operational relevance of co-operative values and principles.

This booklet is not meant to be exhaustive on co-operative governance and it is not a substitute for a co-operative seeking and obtaining independent professional advice.

Co-operative Values and Principles

Co-operatives are unique businesses that are based on explicit values and principles articulated in the International Co-operative Alliance's Statement on the Co-operative Identity adopted in 1995.

Definition

A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise.

Values

Cooperatives are based on the values of self-help, self-responsibility, democracy, equality, equity and solidarity. In the tradition of their founders, cooperative members believe in the ethical values of honesty, openness, social responsibility and caring for others.

Principles

The cooperative principles are guidelines by which cooperatives put their values into practice.

1st Principle: Voluntary and Open Membership

Cooperatives are voluntary organizations, open to all persons able to use their services and willing to accept the responsibilities of membership, without gender, social, racial, political or religious discrimination.

2nd Principle: Democratic Member Control

Cooperatives are democratic organizations controlled by their members, who actively participate in setting their policies and making decisions. Men and women serving as elected representatives are accountable to the membership. In primary cooperatives members have equal voting rights (one member, one vote) and cooperatives at other levels are also organised in a democratic manner.

3rd Principle: Member Economic Participation

Members contribute equitably to, and democratically control, the capital of their cooperative. At least part of that capital is usually the common property of the cooperative. Members usually receive limited compensation, if any, on capital subscribed as a condition of membership. Members allocate surpluses for any or all of the following purposes: developing their cooperative, possibly by setting up reserves, part of which at least would be indivisible; benefiting members in proportion to their transactions with the cooperative; and supporting other activities approved by the membership.

4th Principle: Autonomy and Independence

Cooperatives are autonomous, self-help organizations controlled by their members. If they enter into agreements with other organizations, including governments, or raise capital from external sources, they do so on terms that ensure democratic control by their members and maintain their cooperative autonomy.

5th Principle: Education, Training and Information

Cooperatives provide education and training for their members, elected representatives, managers and employees so they can contribute effectively to the development of their cooperatives. They inform the general public – particularly young people and opinion leaders – about the nature and benefits of cooperation.

6th Principle: Cooperation among Cooperatives

Cooperatives serve their members most effectively and strengthen the cooperative movement by working together through local, national, regional and international structures.

7th Principle: Concern for Community

Cooperatives work for the sustainable development of their communities through policies approved by their members.

Author: International Co-operative Alliance, 1995

The ICA is the international non-government organisation which unites, represents and services co-operatives worldwide. It was established in London, UK, in 1898. It has more than 250 member organisations from over 100 countries and represents more than 760 million individuals.

Co-operative Characteristics

The co-operative values and principles create specific challenges for co-operative governance. Co-operatives throughout Australia share these characteristics:

- Formed by a group of people who have a common need and form a co-operative to help each other.
- The members own the co-operative. The co-operative exists to serve and be used by its members.
- Each member has only one vote irrespective of their use of the co-operative.
- The member owners elect the board and charge it with the responsibility of operating the co-operative on their behalf. The board is accountable to the members.
- The board is elected by the members at a general meeting of the co-operative.

Members may choose to raise capital from external sources but without compromising democratic control.

The capital of the co-operative is contributed in whole or part and is the common property of the members.

These characteristics underpin and inform the principles and practice of co-operative governance. Democratic control is integral to co-operative governance. Crucial to co-operative democracy is that any member can stand for and be elected to the board. There is a risk, however, that the need for qualifications and experience could be sacrificed and the co-operative becomes management-driven. The answer to this dilemma is to co-exist democracy and the necessary qualifications and experiences.

Directors of a co-operative are not neutral. They have a business relationship with and personal goals for the co-operative. It is necessary to:

- Clearly define the role of the board and directors.
- Strive to attract directors with appropriate qualifications and expertise.
- Profile required and desired director competencies.
- Provide ongoing training and development for directors and members.

All co-operatives should consider including in their rules provision for membership of State federations.

Except for very small co-operatives, the members are not expected or desire to participate in all decisions of the co-operative. In electing a board, the

members confer on the board the authority to make decisions. The board is, however, accountable to the members about:

- what decisions have been made
- why the decisions have been made
- what co-operative resources have been used
- what results have been achieved and why

Board and Management

It is critical that the board's functions and what is delegated to management is formalised and disclosed.

This will depend on the size and complexity of and culture of the co-operative.

This formal identification is necessary to understand and accept respective accountability and contributions.

Directors need to understand and accept the distinction and difference between "directing" and "managing." Directors do not participate in day-to-day management. Otherwise, this can blur responsibility of senior managers and make it difficult to hold them accountable.

The board needs to question and control but also support managers. Board members have key obligations as directors. They should fully understand their duties and responsibilities and not be reliant on the Manager/CEO to interpret financial statements and other reports prepared for

The board also needs to recognise the critical importance of remuneration for directors and managers and for the board to be explicit on:

- The objectives of remuneration policy.
- The relationship of the policy to co-operative performance.
- The monetary and non-monetary components of the remuneration policy e.g. salary, fees, non-cash benefits, superannuation contributions, fixed versus performance-based remuneration and termination payments.

Co-operative Board

Ultimate decision making authority and responsibility lies with the board - directing and controlling the affairs of the co-operative on behalf of the members. The board establishes the policies and procedures for the conduct

Members Rights and Responsibilities

Co-operatives are member owned and controlled and, therefore, the rights and responsibilities of members are fundamental to co-operative governance and these should be clearly recognised in:

- The Rules of the co-operative.
- The policies of the co-operative.
- The decision-making processes and decisions of the board.
- Operational processes and decisions.

Member Rights

- Attendance at general meetings.
- Voting in co-operative elections.
- Standing for election to the board and committees.
- Voicing opinions and being listened to.
- Being consulted on key issues and decisions.
- Share in the benefits of economic success.
- Access to member education and training programs.
- Access to honest and open information about the economic performance of the co-operative.
- Expect the business practice to be consistent with co-operative values and principles.
- Being informed about rights and responsibilities as a member.
- Equal treatment with other members.

Member Responsibilities

Abide by the rules of the co-operative.

Use the services of the co-operative.

Not act to the detriment of the co-operative.

Acknowledge and believe that the co-operative is a distinct membership organisation.

Acknowledge and subscribe to the co-operative values and principles.

Participate in co-operative education and training programs.

Ensure the continuance of the co-operative as a co-operative.

Questioning and criticising actions and decisions.

Encouraging others to join the co-operative and use its services.

Membership Disclosure

All members should have equal and timely access to information concerning the co-operative including:

- The financial situation
- Performance
- Ownership
- Governance

Information provided by the co-operative to members and other relevant parties should be:

- Factual
- Timely
- Clear and objective

Include all material information

The annual report to members should include:

- A coherent explanation of the co-operative's performance and prospects.
- This should include an explanation of successes and setbacks.
- The report should also be clearly written so that it is easily understood by members.

Membership Development

A co-operative should promote and practice co-operative values and principles. In practice, therefore, a co-operative should:

Actively provide and promote co-operative education to members, managers and employees.

Actively co-operate with other co-operatives at local, state and national levels.

Actively promote equity and non-discrimination in relation to age, race, nationality, sex, religion and politics.

Actively promote and facilitate member retention and growth.

Actively promote and facilitate member ownership and control.

of the co-operative's affairs. All directors are equally responsible for the Board's actions and decisions.

The notion of independence that informs public debate on the organisation of investor-owned companies is not applicable to co-operatives. It has been argued, for instance, that a majority of the directors of an investor-owned company should be independent. Co-operative values and principles and practices, however, require that a majority of directors should be members of the co-operative as users and beneficiaries.

The board approves policies and directs operational management and delegates to a Manager/CEO who is in charge of daily operations. The board supervises the Manager/CEO who reports to the board.

the board. The board must be able to independently understand the existing and emerging business issues and review and challenge the performance of the co-operative and the Manager/CEO. For this to occur, however, the board needs to agree and understand the scope and detail of information it requires for informed decision-making.

The size of the board should be determined by the size and complexity of the business and what is necessary to enable the board to discharge its duties.

All or most directors should have a business relationship with the co-operative. Each director to be an active and efficient member of a board must:

- Be able to read and interpret financial statements.
- Have a basic understanding of legislation governing co-operatives.
- Have a knowledge of risk measurement and effective management.
- Have a knowledge of and a commitment to co-operative philosophy.
- Have a familiarity with asset liability management.
- Have a sound knowledge and understanding of the co-operative's Rules.
- Have a sound knowledge and understanding of Standing Orders.
- Ensure an effective system of financial control including adequate precautions guarding against fraud and facilitating its discovery.
- Have a familiarity with marketing concepts and approaches.
- The specific duties and responsibilities of the board include:

- Exercising due care and diligence in the performance of their duties e.g. attending board, committee and general meetings.
- Providing input and participating in decisions of the board.
- Reading and evaluating monthly financial statements and other reports.
- Ensuring the co-operative complies with all applicable legislation and regulation.
- Developing and approving co-operative policy.

The board of a co-operative has a unique responsibility to monitor membership policies and practices:

- The number of members joining the co-operative.
- The number of members leaving the co-operative.
- The active status of members.
- Contested elections for the Board and any other committees.
- Co-operative education policies and programs for directors, members and employees.
- Director, member and employee participation rates in co-operative education programs.

The board should acknowledge the importance of co-operative education and training for directors and the Rules should include a requirement for all directors to undertake education and training.

Good Faith

Co-operative directors and employees have an obligation to recognise that the interests of the co-operative and its members have priority over any personal interests.

Not only do directors and employees have an obligation to ensure compliance with legislation and regulation. They owe it to the co-operative to act in good faith in the performance of their duties. The fiduciary responsibilities of directors could be summarised as follows.

- Not to obtain or seek to obtain personal profit from any decision or transaction of the board.

- To exercise highest standards of honesty and integrity.
- To avoid conflicts of interest.
- To be aware of their duties and responsibilities.

Acting in good faith means that a director must act for the benefit of the co-operative and not harm the co-operative to further the director's own interest. Directors must not be in a position where their duties and interests conflict.

Business Judgement Rule

Corporations Law includes a business judgement rule in Section 180 (2). The business judgement rule refers to the care and diligence taken by a director. A director must, therefore, make decisions based on:

- Good faith and proper purpose.
- Informing himself or herself about the subject to the extent that he or she believes is appropriate.
- Rationally believes the judgement to be in the interests of the co-operative.

Operational Management

The Manager/CEO is responsible for the administration and operations of the co-operative - including the supervision of employees.

The duties and responsibilities of the Manager/CEO should be in writing and signed by the Manager/CEO and the Chair of the Board - signifying that the document has been read and will be complied with.

Key responsibilities of the Manager/CEO include:

- Directing and supervising all operations of the co-operative.
- Preparing and proposing policy changes to the board.
- Reporting to the board on the financial condition of the co-operative.
- Establishing and monitoring accounting and administration internal controls.
- Ensuring all accounting records are maintained and up to date.
- Preparing annual operating and cash flow budgets.

- Hiring, supervising, disciplining and terminating employees.
- Planning, recommending and implementing programs and policies.
- Representing the co-operative.

Managing Risk and Internal Controls

The management of risk is fundamental to the ongoing success of a co-operative. The key areas are:

- Liquidity risk
- Market risk

Credit risk

- Data risk

Operations risk

Risk is an activity or function that has uncertain outcomes e.g.

- Products not selling.
- Members cease supplying the co-operative.
- A lack of co-operative leadership.
- Not meeting members needs and expectations.
- Failure to implement and communicate industrial relations policies.

Internal controls are the policies and procedures established and implemented by a co-operative to minimize and monitor operational risks:

- Identifying the risks.
- Assessing the risks.
- Measuring the risks.
- Mitigating the risks.

- Communicating the risks.
- Monitoring the risks.

The board is responsible for ensuring the risks are identified and managed. The internal controls adopted by a co-operative must be reinforced by the co-operative's culture and policies.

The purpose of internal controls can be summarised as to:

- Safeguarding assets.
- Verifying efficiency and effectiveness,
- Preventing fraud.
- Preventing waste.
- Assuring reliability of financial information.

There are two broad types of internal control - administrative and accounting.

Accounting controls - to provide assurance that transactions are authorized and recorded in conformity with accounting principles e.g. daily posting, recording of transactions, sequential number and audit trail.

Administrative control - to provide assurance that lines of authority and responsibility are clear and operational and recording functions are separated e.g. accounting system, written policy and procedure and board approval monitoring and cash control.

- Have significant risks been identified and a risk profile created?
- Is there a risk policy and is this clear including the roles and respective accountabilities?
- Does the board and the Manager/CEO have clear strategies for dealing with these risks?
- How are the processes and controls for identifying, monitoring and dealing with risk adjusted to reflect new or changing risks or operational deficiencies?
- Are authority, responsibility and accountability clearly defined?
- Are the decisions and actions of different parts of the co-operative appropriately co-ordinated?

- Does the co-operative analyse the efficiency and effectiveness of its risk management and internal compliance?
- Does the board receive regular, reliable and timely reports on progress on business objectives and risks?
- Are there established procedures for managers, staff and members to report suspected breaches of legislation and regulation?
- Are there procedures to monitor the effective application of policies, practices and activities related to internal control and risk management?
- Are there appropriate reports to the board on the effectiveness of the ongoing monitoring of risk?
- Does the board review at least annually risk management?

Accounting System

The accounting system should provide the co-operative with complete and accurate financial information.

The basis for this is:

Proper methods for handling members transactions. Accurate recording of transactions in the books and records.

Proper receipt and disbursement of funds.

The co-operative must ensure:

- The maintenance of adequate accounting records.
- That there are suitable accounting policies.
- That reasonable and prudent judgments are used in the preparation of financial statements.
- That applicable accounting standards are followed.
- That any material departures are disclosed and explained in the notes to accounts.
- That adequate systems are in place to comply with legislation.

Financial statements include two principal reports - the balance sheet and the income statement. The balance sheet summarises the co-operative's position

at a point of time. It lists asserts, liabilities and capital accounts. The income statement summarises the income earned and expenses incurred during the period

The balance sheet summarises the co-operative's position at a point of time. It lists assets, liabilities and capital accounts. The income statement summarises the income earned and expenses incurred during the period and whether the co-operative made a profit.

The annual financial reports of the co-operative consist of:

- the financial statements for the year
- the notes to the financial statements
- the directors' declaration about the statements and notes

The financial statements consist of:

- a profit and loss statement for the year
- a balance sheet at the end of the year
- a statement of cash flows for the year

CO-OPERATIVE GOVERNANCE: CHECKLIST

Yes No

CO-OPERATIVE STRUCTURES AND PROCESSES

Statutory Accountability

1	Has the board established effective arrangements to ensure compliance with all applicable legislation and regulations including Co-operatives Act and Corporations Law?	
---	---	--

2	<p>Accountability for Member Funds</p> <p>Has the board established appropriate arrangements to ensure that member funds are:</p> <ul style="list-style-type: none"> ▪ Properly safeguarded? ▪ Used economically, efficiently and effectively? ▪ Used in accordance with the legislative authorities that govern their use? 	
3	<p>Communication with Members</p> <p>Has the board established:</p> <ul style="list-style-type: none"> ▪ Clear channels of communication with members? ▪ Appropriate processes to ensure that these channels operate effectively in practice? 	
4	Has the board made an explicit commitment to openness in all the activities of the co-operative?	
5	<p>Does the board:</p> <ul style="list-style-type: none"> ▪ Report to members the appointing casual vacancies to the board? ▪ Make available the names of all board members, together with their relevant experiences and other interests 	
6	<p>Board and Management Roles and Responsibilities</p> <p>Is there a clearly defined division of responsibilities between the board and management?</p>	

7	<p>Does the board:</p> <ul style="list-style-type: none"> ▪ Meet regularly? ▪ Retain full and effective control over the co-operative? ▪ Effectively and efficiently monitor the management 	
8.1	Has the board established a framework of strategic control (or scheme of delegated or reserved powers)	
8.2	Does the framework of strategic control include a formal schedule of those matters specifically reserved for the decision of the board?	
8.3	Does the board maintain the framework of strategic control up to date?	
9.1	<p>Has the board established clearly documented and understood processes for:</p> <ul style="list-style-type: none"> ▪ Policy development, implementation and review? ▪ Decision-making, monitoring, control and reporting? 	
9.2	Has the board established formal procedural and financial policies to govern the conduct of its business?	
10	Has the board established appropriate arrangements to ensure that it has access to all such relevant information, advice and resources as is necessary to enable it to carry out its role effectively?	
11.1	<p>Has the board established a policy and process for monitoring active membership of the co-operative including:</p> <ul style="list-style-type: none"> ▪ Membership churn – membership retention and acquisition? ▪ Membership activity including economic participation, attendance at general meetings and standing and voting for the board? 	

11. 2	Are all or a majority of directors active users and beneficiaries of the co-operative?	
12	Is the role of the chairman formally defined in writing?	
13. 1	<p>Are any independent directors:</p> <ul style="list-style-type: none"> ▪ Independent of management? ▪ Free from any other relationships which may materially interfere with exercising an independent judgement on issues of strategy, performance, resources and standards of conduct? 	
a1 3.2	Are the duties, terms of office, remuneration and its review of board members defined clearly and in writing?	
14	<p>Are the duties, term of appointment, remuneration and review of management clearly defined and in writing?</p> <ul style="list-style-type: none"> ▪ Are appointments for a fixed term? ▪ Are appointments subject to a formal appraisal process? 	
15. 1	Does the manager have line responsibility for all aspects of executive management?	
15. 2	Is he or she accountable to the board for the ultimate performance and implementation of the board's policy?	
16	Has the board made management responsible for the business being operated consistently with co-operative values and principles?	
17	Has the board made a senior executive responsible for ensuring that board procedures are followed and that all applicable legislation and regulations are complied with?	
18	Has the board established a remuneration committee to make recommendations on the remuneration of top executives?	
19	<p>FINANCIAL REPORTING AND INTERNAL CONTROLS</p> <p>Annual Reporting</p> <p>Does the board publish on a timely basis an objective, balanced and understandable annual report?</p>	

20	Does the board include in its annual report a statement explaining its responsibility for the co-operative's accounts and its adherence to co-operative values and principles?	
21	Does the board include in its annual report a statement confirming that it has complied with relevant standards or codes of co-operative governance?	
22.1	<p>Internal Controls</p> <p>Has the board taken steps to ensure that systems of internal control:</p> <ul style="list-style-type: none"> ▪ Are established? ▪ Continue to operate in practice? 	
22.2	Does the board include in its annual report a statement on the effectiveness of the body's systems of internal control?	
23	Has the board taken steps to ensure that effective systems of risk management are established as part of the systems of internal control?	
24	Has the board taken steps to ensure that an effective internal audit function is established as part of the systems of internal control?	
25	<p>Audit Committee</p> <p>Has the board established an audit committee with responsibility for the independent review of the systems of internal control and the external audit process?</p>	
26	<p>External Auditors</p> <p>Has the board taken steps to ensure that an objective and professional relationship is maintained with the external auditors?</p>	
27	<p>STANDARDS OF BEHAVIOUR</p> <p>Leadership</p> <p>Has the board taken steps to ensure that its directors and managers exercise leadership by conducting themselves in accordance with co-operative values and principles and high standards of personal behaviour?</p>	

28	<p>Code of Conduct</p> <p>Has the board developed a formal code of conduct defining the standards of co-operative values and principles and personal behaviour, to which individual board members and all employees of the co-operative are required to subscribe?</p>	
29	<p>Has the board established appropriate mechanisms to ensure that directors and employees of the body are not influence by prejudice, bias or conflicts of interest?</p>	

This checklist is based on a Good Corporate Governance Checklist developed by The Institute of Internal Auditors (UK and Ireland). It has been amended and/or developed to recognise the co-operative difference and the impact this has on governance.

Second Draft: Wednesday, 11 February 2004

